

- 1.1 Under general tax law some, but not all, expenses payments and benefits are taxable remuneration. Since 1948 the Income Tax law has also contained special rules affecting most directors and employees. The broad effect of these special rules was that expenses payments made to them and benefits provided for them became taxable.
- 1.2 The Finance Act 1976 and subsequent Finance Acts have extended these special rules to a greater number of individuals and provided new arrangements for taxing a variety of benefits provided for directors and certain employees (for example, motor cars, loans and vans).
- 1.3 This booklet describes the scope of the legislation and the effect of the changes resulting from the Finance Act 1976 and subsequent Finance Acts. Most of the relevant provisions are now in Part 3 Chapters 2-11 Income Tax (Earnings and Pensions) Act 2003 (ITEPA 2003).

Unless otherwise stated the statutory references in this booklet are to ITEPA 2003. The full meanings of other abbreviations which also appear in the booklet are:

CAA 2001	Capital Allowances Act 2001
ESC	Extra-statutory concession – followed by its letter and number
FA	Finance Act – followed by year in which enacted
ICTA 1988	Income and Corporation Taxes Act 1988
ITTOIA 2005	Income Tax (Trading and Other Income) Act 2005
SI	Statutory Instrument - followed by its number and the year in which it was made
TMA 1970	Taxes Management Act 1970.

Enquiries

- 1.4 Enquiries by taxpayers (or their agents) about the application of the provisions of ITEPA 2003 to their particular circumstances should be made to the HM Revenue & Customs (HMRC) office dealing with their tax affairs.

The benefits code

Sections 1(1), 62(1), 7(5) and (6)

Sections 63(1) and (2)

- 1.5 In ITEPA 2003 Income Tax is chargeable on employment income that includes:
 - earnings – salary, wages, fees and other emoluments
 - amounts treated as earnings – including the benefits code
 - amounts which are not earnings but count as employment income (see Chapters 23 and 27 of this booklet).

The benefits code concerns expenses payments to, and benefits provided for, directors and employees, subject to limitations for:

- certain directors (paragraph 1.10), and
- where the employment is an **excluded employment** (see paragraph 1.19).

Deductible expenses

Sections 336-338

- 1.6 Directors or employees affected by these provisions will not necessarily have to pay tax on the full amount or value of expenses payments or benefits provided. They may be entitled to a deduction for certain expenses. Further information on this is given in Chapters 7-10 and Chapter 20.

Who is affected?

Section 63(1)

Section 67(1)

Section 216(3)

- 1.7 The benefits code applies to:
 - (a) directors and certain other persons in controlling positions whatever their remuneration, but not to certain full-time working directors and certain directors of charities and non-profit making concerns, and
 - (b) employees, including the directors excluded under (a) above, who are remunerated at the rate of £8,500 or more a year including all expenses payments and benefits before the deduction of any allowable expenses other than:
 - contributions to an approved superannuation fund in respect of which the individual is entitled to tax relief as an expense
 - exempt profit-related pay
 - contributions under an approved payroll giving scheme.

Certain motoring expenses are disregarded for purposes of assessing the car and car fuel benefits described in Chapters 11, 12 and 13. But all these motoring expenses, in addition to the car and fuel benefit charges mentioned in Chapters 11 to 13, must be taken into account for the purposes of the £8,500 test (see paragraph 11.14).

- 1.8 In the remainder of this booklet, unless otherwise indicated the word employee should be read as referring to directors and employees, other than those in an excluded employment (see paragraph 1.19).

Directors

Sections 67(1) and 67(2)

- 1.9 The word **director** includes directors of companies and any person in accordance with whose instructions the directors are accustomed to act (other than a person who is merely a professional adviser). The word **company** includes an unincorporated association.

Section 832

The word director also includes a member of the committee which manages such an association and any member of a body whose affairs are managed by its members. But certain directors of charities or non-profit making concerns are excluded from the special rules as are certain full-time working directors - see paragraph 1.10 to 1.16.

Section 216(3)

Exclusion of certain directors from the special rules

Section 67(3)

- 1.10 A full-time working director is defined as a **director who is required to devote substantially the whole of his or her time to the service of the company in a managerial or technical capacity.**

Sections 66(3) and 66(4) Sections 68(1)

- 1.11 A full-time working director whose rate of remuneration including all expenses payments and benefits has not exceeded, or does not exceed £8,500 a year and who, either as an individual or together with associates and relatives, does not own or control a **material interest** (*broadly more than 5% of the ordinary share capital*) in the company is excluded from the scope of the legislation.

Section 216(3)

- 1.12 Certain directors of charities or non-profit making concerns are also excluded from the special rules. To be excluded, such a director:
- must not own or control directly or indirectly a material interest (see paragraph 1.11) in the company employing him or her, **and**
 - must not be remunerated at a rate of £8,500 or more a year including all expenses payments and benefits before deducting any allowable expenses, **and**
 - must be either
 - a full-time working director as described in paragraph 1.10, **or**
 - a director of a charity or a non-profit making concern.
- 1.13 Even where the director satisfies the above conditions he or she will remain within the scope of the special rules if any of his or her employments with the same employer or with an associated employer is not an excluded employment.

Section 505

Meaning of charity

- 1.14 The word charity as used above means a body **established for charitable purposes only.** A body or concern which has been granted charitable exemption for tax purposes by HMRC Executive Committee will be treated as a charity.

Non-profit making companies

Section 216(3)

- 1.15 A **non-profit making company** is one which does not carry on a trade and whose functions do not consist wholly or mainly in the holding of investments or other property. The mere fact that the concern involved does not make a profit does not make it a non-profit making concern for the purposes of the legislation.

General effect of the exclusions

- 1.16 The general effect of the exclusions is that they remove from the special rules:
- full-time working directors of any concerns
 - members of committees who are treated as directors of unincorporated bodies or non-profit making concerns
 - directors of charities,
- provided that
- the individuals are not remunerated at a rate of £8,500 a year or more calculated in accordance with paragraph 1.7(b), **and**
 - they do not hold a material interest in the body or concern employing them.

This paragraph should be read subject to the reservation in paragraph 1.13 above.

Employees

Section 201(2)

1.17 The special provisions apply to an employee if, for the appropriate tax year, the remuneration together with all expenses payments made to him or her and benefits provided for him or her amounts in all to £8,500 or more a year before deducting any expenses allowable for Income Tax. The special rules also apply to any of the full-time working directors or directors of charities or non-profit making concerns excluded under paragraphs 1.11 to 1.16 whose rate of remuneration is similarly £8,500 or more a year.

Section 220

1.18 In this connection, all employments held by an individual under the same employer are treated as a single employment for the purposes of the £8,500 remuneration limit. Similarly, where an individual holds a number of employments with interconnected companies, these employments are regarded as if they were one employment for the purpose of deciding whether the individual is paid at a rate of £8,500 or more. And if any of the individual's employments with the same employer or with an associated employer is not an excluded employment, the individual will be within the scope of the special rules in respect of all those employments.

Exclusion of certain employees from the special rules

Section 63(4)

Section 216(1)

Section 63(2)

1.19 If an employee's remuneration does not amount to £8,500 or more a year, the employment is a lower paid employment. In this context the term employee does not apply to a director (paragraph 1.8). A lower paid employment is an excluded employment to which the special rules in the benefits code do not apply, with the exception of the provision of living accommodation and vouchers or credit-tokens.

Meaning of employment

Section 66(3)

1.20 The word employment as used in this booklet means any office or employment whose earnings are chargeable as employment income.

Meaning of remuneration

1.21 For simplicity, the word **remuneration** has been generally used in this booklet in place of the word **earnings** in ITEPA 2003 and means any kind of pay for a job. It includes salaries, fees, pay, wages, overtime pay, leave pay, bonus, commission, perquisites, tips, gratuities, benefits in kind and expenses payments and allowances.

Benefits provided for the family or household of an employee

Section 201(1)

Section 721(5)

Section 174(6)

Section 839

1.22 Subject to minor exceptions any benefit provided for the members of the family or household of an employee ranks as if it were provided for the employee personally. The term family or household covers the employee's:

- spouse
- children and their spouses
- parents
- servants, dependants and guests
- registered civil partner.

Where benefits are provided in connection with loans and share incentive schemes there are different definitions of the family circle. For beneficial loan arrangements see paragraph 17.10.

Provision of benefits by employer

Sections 201(3) and 117

1.23 Where expenses payments are made to, or benefits are provided for, an employee or members of the employee's family or household by the employer they are deemed to have been made or provided by reason of that employment - they are regarded as part of the reward for the job.

Section 201(3) - proviso

1.24 There is one statutory exception to this - where the employer is an individual and a benefit provided by the employer has been made in the normal course of domestic, family or personal relationships. In addition, paragraph 11.10 gives details of certain exemptions which apply where a company provides cars for two or more members of the same family.

Provision of benefits by someone other than the employer

Section 201(2) Section 209

1.25 Benefits provided for employees (or members of their families or households) by reason of their employment by someone other than their employer are taxable in the same way as if they had been provided by their employer.

Section 554A

1.26 Finance Act 2011 introduced new rules in Part 7A ITEPA 2003, which apply in certain circumstances where there are arrangements to use third parties to reward employees. These rules are sometimes referred to as the 'disguised remuneration' regime. Broadly speaking, if third party arrangements are used to provide for what is in substance a reward or recognition, or a loan, in connection with the employee's current, former or future employment, then an Income Tax charge arises and the amount concerned will count as employment income.

Sections 554A, 554B, 554C and 554D

1.27 The rules only apply where a defined step is taken through a 'relevant third person'.

Section 554A

1.28 The direct employer is not a 'relevant third person' unless it is acting as a trustee.

Section 554A

- 1.29 A company that is a member of the same group of companies as the employing company at the time the step is taken is **not** a 'relevant third person' unless:
- the step is taken as part of a tax avoidance arrangement, or
 - the group company is acting as a trustee.

Sections 554Z(5) and (6)

- 1.30 In determining whether two companies are members of the same group for this purpose, a special test is used. This test applies the group membership rules for Corporation Tax on chargeable gains, with one modification. The chargeable gains test is a 75% test. For the purposes of the group exception, use 51% instead of 75%. But otherwise the test works the same way.

Sections 554E to 554X inclusive

- 1.31 The rules in Part 7A ITEPA contain detailed exclusions. These prevent the legislation from catching certain arrangements, even where there is a 'relevant third person' involved. Generally the exclusions are targeted at arrangements which are not tax avoidance arrangements. The exclusions are subject to conditions and cover topics such as employee share and share option schemes, employee car ownership schemes, certain pension schemes and transactions under employee benefit packages.
- 1.32 For more information on the new rules, please refer to the CWG2(2012), Chapter 5, paragraphs 166 to 167 titled *Employment income provided through third parties ('Disguised Remuneration' rules)*.

Sections 418(2) and (3) ICTA 1988

Close companies – treatment of benefits

- 1.33 A benefit which falls within the special provisions described in this booklet is excluded from the extended definition of **distribution** for **close companies** which normally includes benefits in kind afforded to a participator or to an associate of a participator.

Part XI, Chapter I ICTA 1988

- 1.34 Broadly speaking, a **close company** is one under the control of five or fewer participators and their associates or of directors who are participators and their associates. There are special definitions for this purpose of **control**, **participator** and **associate**.

There are exceptions, for example, a company whose shares are quoted on the Stock Exchange is not normally close if 35% or more of its shares are held by the general public.